Internal Revenue Service

memorandum

CC:TL-N-151-89
Br2:RLOsborne

date: DEC 8 1988

to: District Counsel, Cleveland CC:CLE
Attention: Robert Kern

from: Assistant Chief Counsel (Tax Litigation) CC:TL

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subject: Proper Agent for Execution of Forms 872 -- [redacted]

We hereby respond to your September 29, 1988, request for technical advice.

ISSUE

Who should sign Forms 872 for [redacted] ("[redacted]") for the taxable year ending [redacted], in light of changes in [redacted]'s corporate structure at the end of [redacted]?

FACTS

We understand that prior to [redacted], [redacted], a Michigan corporation, was the common parent of an affiliated group ("the [redacted] group") filing consolidated income tax returns. On that date [redacted] merged with [redacted] ") in a leveraged buyout. [redacted] was wholly-owned by [redacted], which was in turn wholly-owned by [redacted]. [redacted], [redacted] and [redacted] were all Delaware corporations. In the merger, [redacted] went out of existence and [redacted] survived as the new wholly-owned subsidiary of [redacted]. The shareholders of [redacted] were bought out with cash borrowed by the [redacted] group.

On the same date, [redacted], [redacted] merged with [redacted]. [redacted] went out existence and [redacted] survived as the continuing subsidiary of [redacted] then changed its name to [redacted] but remained a Delaware corporation.

Currently, the [redacted] group is under audit for the taxable year ending [redacted]. The statute of limitations on assessment for that year was purportedly extended on [redacted] by a consent signed by [redacted], Vice President, [redacted]. The current extension expires [redacted]. You have asked us to assume that the [redacted], consent was executed before the period of limitations expired. You have asked whether the form of that consent is

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defensible, and who should sign future consents for years prior to the mergers.

DISCUSSION

Treas. Reg. § 1.1502-77(a) provides that a group's common parent shall be the group's sole agent for waiver purposes with respect to the group's consolidated return year. Accordingly, if a waiver relating to a given year is needed subsequently, after a restructuring, as a general rule the entity which was previously the common parent continues to act as agent for the signing of the waiver. This is the case even if the former common parent is no longer the common parent at the time it signs the waiver.

The general rule set forth above does not apply, however, where the restructuring results in the termination of the existence of the common parent. In that event, Reg. § 1.1502-77(d) provides that the new agent for the group will be either (1) a member designated by the old common parent prior to the termination of its existence, or (2) a member designated by the remaining members of the group if the old common parent failed to make a designation. That regulation further provides that if neither the old common parent nor the remaining members designate a new agent, the district director must deal with the members on an individual basis.

Finally, Southern Pacific Co. v. Comm'r, 84 T.C. 375 (1985), provides another rule for reverse acquisitions under Reg. § 1.1502-75(d)(3)(i). That regulation applies where one corporation acquires a second corporation, and the acquired corporation's shareholders receive stock in the acquiring corporation, so that the acquired corporation's shareholders have more than 50% of the value of the stock of the acquiring corporation immediately after the acquisition. The regulation provides that the acquired corporation's affiliated group is deemed to continue in existence, with the acquiring corporation as the new common parent. Southern Pacific involved a reverse acquisition in which the old common parent went out of existence as a corporation. The Tax Court held that under the circumstances the new common parent automatically became the common parent for pre-reorganization years as well as for future years. Tax Litigation Division interprets this rule to apply to reverse acquisitions only where the old common parent goes out of existence as a corporation.

The merger of [redacted] with [redacted] would probably be treated as a purchase of [redacted]'s stock by [redacted]. Rev. Rul. 79-273, 1979-2 C.B. 125; Rev. Rul. 73-427, 1973-2 C.B. 301. The shareholders of [redacted] (the acquired corporation) received cash, not stock in [redacted] (the acquiring corporation). Accordingly, the merger does not appear to be a reverse acquisition within the meaning of Reg. 1.1502-75(d)(3)(i).

Accordingly, the rule of Southern Pacific does not apply.

There is some case authority to argue that when [redacted], the old common parent, merged into [redacted], the identity of [redacted] continued in the form of [redacted] (under the new [redacted] name). Helvering v. Metro Edison Co., 306 U.S. 522 (1939). Under such reasoning, it could be argued that the new [redacted] was the proper successor party to sign a Form 872 on behalf of the group after the merger under Reg. 1.1502-77(a).

In our view, however, the argument set forth above is unlikely to prevail in litigation. The case authority for that argument developed in the absence of specific controlling provisions in the Internal Revenue Code and Treasury Regulations as to who could take deductions of a terminating corporation. In contrast, Reg. 1.1502-77(d) specfically prescribes which entities may be agent in the event the common parent terminates. Under § 21.200(721) of the Michigan Business Corporation Act, when two corporations merge, all the constituent corporations cease to exist except the corporation which the parties designate as the surviving corporation.[1] Accordingly, following the [redacted], merger of [redacted] into [redacted], [redacted] (the Michigan corporation), the old common parent, ceased to exist. [2] Regulation 1.1502-77(d) does not provide for the agency power to pass to a successor-in-interest. It merely provides that unless there has been a formal designation of a new agent by the old common parent or the other group members, the district director must deal with the group members individually. In this case neither [redacted] nor its subsidiaries ever designated a new agent. Accordingly, the [redacted], consent by new [redacted] would probably not be upheld by a court to the extent that it purports to bind all members of the old [redacted] group.

Although we probably would not prevail with respect to group members on a successor agency theory, we have a stronger argument that the [redacted] consent at least bound the new [redacted] itself. As successor-in-interest to the old [redacted], under state law new [redacted] has individual liability for the old [redacted]'s obligations, even if new [redacted] is not an agent for the group under Reg. 1.1502-77(d).[3] Such obligations include old [redacted]'s tax obligations.

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[1] A merger is to be contrasted with a dissolution, in which the dissolving corporation is deemed to continue in existence for purposes of winding up. Michigan Business Corporation Act, § 21.200(833).

[2] The [redacted] that currently exists (a Delaware corporation) and the original [redacted] (a Michigan corporation) are different corporations.

[3] 8 Delaware Code § 259(a).

Moreover, since the old [redacted] was individually liable for the tax liability of the entire old [redacted] group, the new [redacted] would similarly be liable to pay the tax obligation of the entire old [redacted] group.

The argument above has two shortcomings. First, the [redacted], consent does not specify that [redacted] was executing the consent as a successor-in-interest. Second, because the consent would not bind other members of the group, the Service could not reach the assets of any such members which are no longer subsidiaries of [redacted]. Nonetheless, for the limited purpose of reaching new [redacted]'s assets (including [redacted]'s stock in its current subsidiaries), it is an argument that we should be prepared to assert if necessary.

The [redacted], consent expires [redacted], and we understand that more time will be needed to complete the audit. Although we would have recommended a different original consent in [redacted], at this point we recommend that you obtain a single renewal consent from new [redacted] in exactly the same form that was used for the [redacted] consent. As we have explained, we doubt that a court would uphold such a consent as an assertion of agency power. However, obtaining a renewal consent executed by [redacted] as agent at this point would not appear to do any harm. If the [redacted] consent is invalid as an assertion of agency power, the three-year statute has now expired for the group members regardless of how the renewal consent is executed. Moreover, expiration of the statute of limitations must be raised by taxpayers as an affirmative defense. The taxpayers here might not think to assert the statute of limitations on the basis that the [redacted] consent was invalid as an agent consent. Indeed, to abandon the agency approach at this point might unnecessarily alert the group members to the potential vulnerability of the [redacted] agent consent.

We have considered the possibility of obtaining (1) a second [redacted] renewal consent with language describing [redacted] as a succesor to old [redacted]; (2) additional Forms 872 from individual subsidiaries which are no longer [redacted] affiliates; and (3) a transferee consent by new [redacted] on Form 977. We have decided that these measures would be undesirable primarily because they might unnecessarily alert the taxpayers to the potential vulnerability of the [redacted] consent. Moreover, as we discuss below, such measures would not provide additional protection.

With respect to successorship language, if the wording on the [redacted] consent was insufficient to extend the statute of limitations for new [redacted] individually as a successor, the statute of limitations has now expired regardless of how the renewal consent is worded. If the wording on the [redacted] consent was sufficient, on the other hand, it presumably will be equally sufficient on the renewal consent.

With respect to former [redacted] affililates, if the [redacted] consent was invalid as an assertion of [redacted]'s agency power, the statute of limitations has already expired on such group members, and it cannot be resurrected by separate consents at this point. On the other hand, if the [redacted] consent was valid as an assertion of [redacted]'s agency power, and the agency consent is renewed, separate consents from former members would appear to provide no additional benefit, since such former members would already be bound by the agent consent.

Finally, with respect to transferee liability, if the [redacted], Form 872 is invalid, transferee liability apparently expired in [redacted] of this year. On the other hand, if the [redacted], Form 872 is valid, and another Form 872 is executed at this time to extend the limitations period further, transferee liability would appear to provide no additional benefit beyond the benefit already inherent in individual successorship liability.

CONCLUSION

There is a good possibility that the [redacted], consent would not be upheld by a court to the extent that it purports to bind all members of the old group. However, the [redacted] consent is probably sufficient to bind new [redacted] individually as successor-in-interest. We recommend that if additional time is needed to complete the subject audit, any additional consents be executed in the same form as the [redacted] consent.

MARLENE GROSS

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